

A hand with pink nail polish holds a small, glowing pile of dark brown, granular rare earth minerals. The background is a larger pile of the same material, creating a sense of depth. The lighting is warm and golden, highlighting the texture of the minerals and the hand. Several chemical element ratios are scattered across the image, including Tm/Yb/Y/Lu, Sm/Eu/Gd, La/Ce/Pr, Tb/Dy/Ho/Er, and La/Ce/Pr/Nd.

## INTERIM REPORT 2002



中國稀土控股有限公司  
China Rare Earth Holdings Limited  
(Incorporated in the Cayman Islands with limited liability)



The Board of Directors (the “Board”) of China Rare Earth Holdings Limited (the “Company”) is pleased to announce the unaudited consolidated interim results of the Company and its subsidiaries (the “Group”) for the six months ended 30th June 2002 together with the comparative figures for the corresponding period in 2001 as follows:

## ■ CONDENSED CONSOLIDATED INCOME STATEMENT

	<b>For the six months ended 30th June</b>	
	<b>2002</b>	<b>2001</b>
	<b>(Unaudited)</b>	<b>(Unaudited)</b>
	<b>HK\$'000</b>	<b>HK\$'000</b>
Turnover	<b>196,113</b>	333,059
Cost of sales	<b>(138,463)</b>	(226,557)
Gross profit	<b>57,650</b>	106,502
Other revenue	<b>3,187</b>	2,903
Selling and distribution costs	<b>(5,988)</b>	(6,581)
Administrative expenses	<b>(10,051)</b>	(17,321)
Other income (expenses), net	<b>256</b>	(2,725)
Profit from operations	<b>45,054</b>	82,778
Finance costs	<b>(3)</b>	(1,275)
Profit before taxation	<b>45,051</b>	81,503
Taxation	<b>(6,137)</b>	–
Profit after taxation	<b>38,914</b>	81,503
Minority interests	<b>(996)</b>	(2,880)
Net profit for the period	<b>37,918</b>	78,623
Dividends	<b>16,289</b>	20,773
Basic earnings per share	<b>4.66 cents</b>	11.46 cents



## ■ CONDENSED CONSOLIDATED BALANCE SHEET

	30th June 2002 (Unaudited) HK\$'000	31st December 2001 (Audited) HK\$'000
PREPAYMENT FOR AN INVESTMENT IN A SUBSIDIARY	—	100,000
FIXED ASSETS AND CONSTRUCTION- IN-PROGRESS	407,798	325,242
CURRENT ASSETS		
Inventories, net	190,062	165,539
Accounts receivable and other receivables, net	92,221	118,861
Prepayments, deposits and other current assets	26,336	56,756
Due from related companies	1,659	1,463
Pledged deposits	4,246	1,081
Cash and cash equivalents	320,940	247,936
	635,464	591,636
CURRENT LIABILITIES		
Accounts payable	22,522	22,162
Accruals and other payables	51,804	38,730
Taxation payable	6,925	2,427
Due to directors	1,282	13,906
Due to related companies	269	1,856
	82,802	79,081
NET CURRENT ASSETS	552,662	512,555
MINORITY INTERESTS	17,065	16,069
NET ASSETS	943,395	921,728
CAPITAL AND RESERVES		
Share capital	81,445	81,445
Reserves	861,950	840,283
SHAREHOLDERS' EQUITY	943,395	921,728



## ■ CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For the six months  
ended 30th June

	2002 (Unaudited) HK\$'000	2001 (Unaudited) HK\$'000
Net cash generated from operating activities	71,762	59,417
Net cash generated from (used in) investing activities	1,204	(69,610)
Net cash generated from financing activities	—	6,405
Increase (decrease) in cash and cash equivalents	72,966	(3,788)
Cash and cash equivalents at beginning of period	247,936	122,550
Effect of foreign exchange rate changes	38	74
Cash and cash equivalents at end of period	<u>320,940</u>	<u>118,836</u>
Analysis of cash and cash equivalents:		
Cash and bank balances	<u>320,940</u>	<u>118,836</u>



## ■ CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital HK\$'000	Share premium HK\$'000	Capital reserve HK\$'000	Statutory reserves HK\$'000	Exchange translation reserve HK\$'000	Retained profit HK\$'000	Total HK\$'000
As at 1st January 2002	81,445	412,485	32,837	26,968	3,499	364,494	921,728
Net gains not recognized in the income statement:							
Exchange differences on translation of the financial statements of foreign entities	-	-	-	-	38	-	38
Net profit for the period	-	-	-	-	-	37,918	37,918
Dividends declared during the period	-	-	-	-	-	(16,289)	(16,289)
Appropriations to statutory reserves	-	-	-	8,155	-	(8,155)	-
As at 30th June 2002	<u>81,445</u>	<u>412,485</u>	<u>32,837</u>	<u>35,123</u>	<u>3,537</u>	<u>377,968</u>	<u>943,395</u>
As at 1st January 2001	67,529	130,958	32,837	11,593	3,218	274,718	520,853
Net gains not recognized in the income statement:							
Exchange differences on translation of the financial statements of foreign entities	-	-	-	-	176	-	176
Net profit for the period	-	-	-	-	-	78,623	78,623
Dividends declared during the period	-	-	-	-	-	(20,773)	(20,773)
Appropriations to statutory reserves	-	-	-	8,642	-	(8,642)	-
Issue of shares	3,396	37,338	-	-	-	-	40,734
Share issue expenses	-	(9)	-	-	-	-	(9)
As at 30th June 2001	<u>70,925</u>	<u>168,287</u>	<u>32,837</u>	<u>20,235</u>	<u>3,394</u>	<u>323,926</u>	<u>619,604</u>



## ■ NOTES TO THE CONDENSED FINANCIAL STATEMENTS

### 1. Principal accounting policies

The unaudited condensed financial statements have been prepared under the historical cost convention and in accordance with the Statement of Standard Accounting Practice ("SSAP") No. 25 "Interim financial reporting" issued by the Hong Kong Society of Accountants and Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules").

The accounting policies adopted are consistent with those followed in the Group's annual financial statements for the year ended 31st December 2001 except that the Group has changed certain of its accounting policies following its adoption of the following new and revised SSAPs which are effective for accounting periods commencing on or after 1st January 2002:

SSAP 1 (revised):	Presentation of financial statements
SSAP 11 (revised):	Foreign currency translation
SSAP 15 (revised):	Cash flow statements
SSAP 25 (revised):	Interim financial reporting
SSAP 34:	Employee benefits

The new and revised SSAPs have introduced revised disclosure requirements which have been adopted in the condensed financial statements. Comparative figures for prior period have been restated in order to achieve a consistent presentation. The adoption of the above SSAPs has had no significant effect on the results for the current or prior accounting periods.



## 2. Segment information

### a. Business segments

	For the six months ended 30th June	
	2002 (Unaudited) HK\$'000	2001 (Unaudited) HK\$'000
Revenue		
– Rare earth products	71,786	212,133
– Refractory products	124,327	120,926
	<u>196,113</u>	<u>333,059</u>
Results		
– Rare earth products	15,252	58,152
– Refractory products	33,161	30,922
	<u>48,413</u>	<u>89,074</u>
Unallocated corporate expenses, net	(6,546)	(9,199)
Other revenue	<u>3,187</u>	<u>2,903</u>
Profit from operations	45,054	82,778
Finance costs	(3)	(1,275)
Profit before taxation	<u>45,051</u>	<u>81,503</u>

### b. Geographic segments

	Turnover For the six months ended 30th June	
	2002 (Unaudited) HK\$'000	2001 (Unaudited) HK\$'000
The Peoples' Republic of China ("the PRC")	126,545	174,471
Japan	39,850	86,314
The United States	15,071	50,922
Others	14,647	21,352
	<u>196,113</u>	<u>333,059</u>

Certain of the sales to foreign countries were conducted through import/export agents in the PRC on a back-to-back basis.



### **3. Depreciation**

During the period, depreciation of HK\$13,019,000 (2001: HK\$9,386,000) was charged in respect of the Group's fixed assets.

### **4. Interest on borrowings**

During the period, interest on borrowings of HK\$3,000 (2001: HK\$1,275,000) was charged before profit before taxation.

### **5. Taxation**

Taxation represents PRC Enterprise Income Tax ("EIT") charged for the period.

The PRC subsidiaries of the Company are subject to EIT based on assessable profits in the PRC. Pursuant to the relevant tax laws in the PRC, the two subsidiaries in the PRC, namely Yixing Xinwei Leeshing Rare Earth Company Limited and Yixing Xinwei Leeshing Refractory Materials Company Limited, are entitled to full exemption from EIT during the period from 1st January 2000 to 31st December 2001 and are subject to EIT at a rate of 12% during the period from 1st January 2002 to 31st December 2004. Save as disclosed, all other subsidiaries of the Company in the PRC currently enjoy tax holidays.

No provision for Hong Kong profits tax has been made as the Group had no assessable profits in Hong Kong during both periods.

### **6. Dividends**

During the period, final dividend of the previous year at HK\$0.02 (2001: HK\$0.03) per ordinary share was declared and paid, amounting to a total of HK\$16,289,000 (2001: HK\$20,773,000).

Subsequent to 30th June 2002, the Board has resolved to declare an interim dividend at HK\$0.01 (2001: HK\$0.02) per ordinary share amounting to a total of HK\$8,145,000 (2001: HK\$16,289,000).

The amount of interim dividend has been calculated on the basis of 814,453,059 shares in issue as at 19th September 2002.

### **7. Earnings per share**

Basic earnings per share was calculated based on the net profit for the period of approximately HK\$37,918,000 (2001: HK\$78,623,000) and the weighted average number of ordinary shares of approximately of 814,453,000 (2001: 686,036,000) in issue during the period.

There was no diluted earnings per share shown for the six months ended 30th June 2002 as there was no dilutive potential ordinary shares as at 30th June 2002.





## 8. Fixed assets and construction-in-progress

During the period, the Group spent approximately HK\$95,631,000 (2001: HK\$72,654,000) on acquisition of fixed assets and construction-in-progress.

## 9. Accounts receivable and other receivables

The Group offers an average credit term of 30 to 90 days to eligible trade customers.

As at the end of the period, accounts receivable and other receivables comprised:

	<b>30th June 2002 HK\$'000</b>	31st December 2001 HK\$'000
Accounts receivable	<b>77,695</b>	115,686
Other receivables	<b>24,207</b>	15,209
	<b>101,902</b>	130,895
Less: Provision for bad and doubtful debts	<b>(9,681)</b>	(12,034)
	<b>92,221</b>	118,861

The aging analysis of accounts receivable is as follows:

	<b>30th June 2002 HK\$'000</b>	31st December 2001 HK\$'000
Within 6 months	<b>66,044</b>	103,856
Over 6 months but within 1 year	<b>3,352</b>	2,464
Over 1 year but within 2 years	<b>1,101</b>	1,189
Over 2 years	<b>7,198</b>	8,177
	<b>77,695</b>	115,686



## 10. Accounts payable

The aging analysis of accounts payable as at the end of the period is as follows:

	30th June 2002 HK\$'000	31st December 2001 HK\$'000
Within 6 months	21,484	18,371
Over 6 months but within 1 year	838	2,512
Over 1 year but within 2 years	200	1,057
Over 2 years	—	222
	<u>22,522</u>	<u>22,162</u>

## 11. Capital commitment

As at 30th June 2002, the Group has commitment for capital expenditure in respect of acquisition of equipment and machinery and construction of buildings contracted for but not provided in the financial statements at approximately of HK\$23,523,000 (31st December 2001: HK\$90,303,000).

## ■ MANAGEMENT DISCUSSION AND ANALYSIS

### Financial results

For the six months ended 30th June 2002, the Group recorded a turnover of HK\$196,113,000, representing a drop of 41% from the HK\$333,059,000 recorded in the previous corresponding period. Sales of rare earth products accounted for 37% of total turnover, at HK\$71,786,000, decreased by 66% against the HK\$212,133,000 recorded during the corresponding period last year. Sales of refractory products reached HK\$124,327,000, recording a growth of 3% as compared to HK\$120,926,000 recorded in the same period of last year.

By the end of last year, two subsidiaries of the Group, Yixing Xinwei Leeshing Rare Earth Company Limited and Yixing Xinwei Leeshing Refractory Materials Company Limited, reached the end of their full exemption periods for the PRC Enterprise Income Tax. Commencing this year, both companies are entitled to a 50% relief of such tax. After deducting taxation and minority interests, net profit for the review period reached HK\$37,918,000, falling 52% against the previous corresponding period. Net profit margin reduced to 19%. Basic earnings per share was at HK4.66 cents.



## **Business review**

### *Rare earth business*

The continued worldwide economic slowdown has pushed different industries into an economic trough. The rare earth industry, providing essential materials for production in various industries, also deteriorated in view of the sluggish economic environment. In particular, the shrinkage of the information technology sector significantly dragged down the demand for rare earth products. Additionally, the delay in the confirmation of the State's policy for rare earth sector delayed the release of the export quota for foreign trading companies, which further intensified the difficulty within the industry. Some of the weaker manufacturers in the PRC have had to cease productions under these detrimental conditions. Compared to the last corresponding period, the whole country's rare earth product exports have dropped almost 50% during the first half of 2002, with product prices generally adjusted downwards.

During the period under review, the Group was inevitably affected by these unfavorable external factors, leading to decreases in the production and sale of rare earth products. The Group's sales of rare earth products reached approximately 1,850 tonnes, a decrease of approximately one-half from the 3,500 tonnes recorded in the last corresponding period. In light of the selling price, the majority of the Group's products were also adversely influenced by the market. For instance, the average price of Neodymium Oxide and Dysprosium Oxide during the first half of this year dropped by approximately 40% when compared to the latter half of last year. Lanthanum Oxide also recorded a drop of about 10% in its selling price. During the period, the Group's gross profit margin in the rare earth business was approximately 22%, which was lower than the 28% recorded in the last corresponding period. This was mainly due to the price falls with average cost also increasing in view of the overall decrease in production and sales. Building on the Group's outstanding production technology as well as its economy of scales, it has been able to outperform the industry in achieving significant cost efficiencies. This has allowed the Group to maintain a profit under the harsh environment and to avoid the risk of ceasing operations, a position suffered by many other players in the industry.

The Group has been placing extra effort into developing more value added products to raise profit margins and to meet different customers needs. In May 2002, the 500 tonnes trichromatic phosphor production line at Wuxi Xinwei Fluorescent Materials Company Limited of the Group commenced operation. This move allowed the Group to become one of the largest fluorescent material manufacturers in the PRC.



The new production line mainly produces single RE phosphors, 2,700K – 8,000K trichromatic mixture phosphors, super afterglow phosphors, CTV phosphors, etc. Being environmentally friendly, cost-effective, safe and convenient, these materials are extensively employed in illumination, building materials, fire facilities, railways, highways and commercial buildings, effectively enhancing the performance of products. Apart from sales in the PRC, products will also be sold to overseas markets in the United States, Germany and Japan, etc.

As the production line was newly developed in May, the Group is still conducting trial production. However, orders and the number of enquiries have been stepping up. In view of the positive market response, it is expected to contribute to the Group's annual results.

#### *Refractory business*

The refractory business further magnifies its supporting function during the slackened economic times. During the period under review, the Group's turnover and profit from the refractory business both accounted for over 60% of the Group's total business, resulting such business to become the Group's major source of revenue.

The global economic slowdown and slackened steel and glass industries also exerted pressure on the Group's refractory business. Facing severe foreign competition, large-scale steel manufacturers in the PRC had to tighten the production costs and requested suppliers to cut the price of raw materials. Despite this, market demand for refractory products was still very strong, helping the Group to achieve a stable income with a gross profit margin maintained at over 30%. During the period, the Group's sales of refractory products amounted to 26,000 tonnes, increasing by approximately 6,000 tonnes against the last corresponding period.

The Group's refractory products are mainly sold in the PRC with some exports to overseas like Japan. The Group has been working to increase export sales. During the first half of 2002, the Group's export sales for refractory products reached 18% and is expected to increase even further in the latter half of this year.



In June 2002, the Group's second phase expansion for refractory products commenced operation. This escalated the Group's production capacity by 60% to reach 80,000 tonnes per year. The new production facilities, equipped with advanced and energy-saving production technology and automated control systems, places the Group in an industry leading position as it becomes one of the most scalable of its kind in the PRC. The technological improvements allow the Group to work in cooperation according to the agreement signed between the Group and a Japanese refractory specialist company in April 2001 to jointly develop more new products. These developments have further boosted the Group's brand name and its leading position in the market. The contribution from this new facility is expected to be reflected in the year's final results.

### **Liquidity and financial resources**

As at 30th June 2002, the Group had cash and bank balances of HK\$325,186,000 with nil long-term liabilities. The cash and bank balances included pledged deposits of HK\$4,246,000 that placed with a bank as security against the issuance of certain letters of credit. The unused banking facilities for trade finance amounted to approximately HK\$21,462,000.

Total liabilities to total assets ratio was maintained at 8%.

### **Prospects**

It is impossible for a business to enjoy rapid development all the time without suffering the unpleasant influences of unfavorable external factors. Building on our established business foundations, well-planned expansions in production capacity and enhancements in production technology to improve product quality, our commitment to nurture professionals and maintain desirable customer relationships, the Group has been able to maintain production level and profitability in these harsh economic times and to further expand its business scope and market share by the time of recovery.

The Group will continue to strengthen its research and development capabilities, boosting cooperation between the Group and prominent research institutions in the PRC to ensure leading technology and quality rare earth products, refractory products and fluorescent materials to lead the industry and add value to the Group's products. The Group is also committed to producing more value added products and which is expected to become a significant source of profit for the Group.



With the PRC government's increasing involvement in the management of the rare earth industry, the Group is actively seeking to position itself as the core enterprise in the Southern group of the rare earth management alliance to gain more policy support in the future. At the same time, the Group has formed strategic alliances with areas such as Jiangxi and Guangdong, etc, to stabilize and guarantee the supply of raw materials. Additionally, the Group has been strengthening its cooperation with a state-owned enterprise in the Northern PRC, which is also a leading rare earth supplier in China specializing in the extraction of rare earth refined ore, to stabilize the demand-supply situation for its rare earth products and the price of raw materials.

Currently, there has been a slowdown in the macro-adjustments for the rare earth industry led by the PRC government. The rare earth industry is currently experiencing a period of consolidation as weak players leave the market. In view of the situation, the Group is enhancing its strengths to meet future challenges. The Group will therefore withstand the harsh times remaining well-equipped to benefit from the market rebound.

In the refractory products business, the Group will further widen its scope of cooperation with Japanese refractory specialists, to develop more new products to meet the demands of customers both from the PRC and overseas.

## ■ INTERIM DIVIDEND

The Board has resolved to declare an interim dividend of HK1 cent per share to the shareholders whose names appear on the register of members on 22nd October 2002 for the six months ended 30th June 2002 and payable on or before 1st November 2002.

## ■ CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed at 21st October 2002 and 22nd October 2002, during which period no transfer of shares will be registered. In order to qualify for the above declared interim dividend, all transfers accompanied by the relevant share certificates, must be lodged with the Company's Share Registrars in Hong Kong, Computershare Hong Kong Investor Services Limited, Rooms 1712-1716, Hopewell Centre, 183 Queen's Road East, Hong Kong for registration not later than 4:00 p.m. on 18th October 2002.



## ■ DIRECTORS' INTERESTS IN SHARES

As at 30th June 2002, the interests of the directors and chief executives in the share capital of the Company and its subsidiaries as recorded in the register maintained by the Company pursuant to Section 29 of the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance") were as follows:

### 1. The Company

Director	Nature of interests	Number of shares held
Qian Yuanying	Corporate interests (Note 1)	420,050,000
Huang Chunhua	Personal interests	2,868,000

### 2. Subsidiaries

- (a) Xinwei Rare Earth Group (Hong Kong) Limited

Director	Nature of interests	Number of non-voting deferred shares held
Jiang Quanlong	Personal interests	7,000,000
Qian Yuanying	Personal interests	3,000,000

- (b) Yixing Xinwei Leeshing Rare Earth Company Limited

Director	Nature of interests	Equity interests
Jiang Quanlong	Corporate interests (Note 2)	5%

Notes:

- These shares are held through YY Holdings Limited, the entire issued share capital of which is held by the trustee of the Jiang family trust, the discretionary object of which is a company wholly owned by Ms. Qian Yuanying and her children.
- The equity interest is held by Xinwei Group Limited, a domestic enterprise 5% owned by Mr. Jiang Quanlong with remaining 95% owned by a brother of Ms. Qian Yuanying. Mr. Jiang is also the legal representative of the enterprise.



## ■ DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

There was a Share Option Scheme which was approved by the shareholders of the Company, under which the directors may, at the discretion, invite any full time employee or executive director of the Company or its subsidiaries to take up options at HK\$1 each as a consideration for option to subscribe for shares in the Company.

As at 30th June 2002, no such options had been granted to the directors.

At no time during the six months ended 30th June 2002 was the Company or any of its subsidiaries a party to any arrangement, which enable any of the directors or chief executives of the Company or their spouses or children under the age of 18 to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

## ■ SUBSTANTIAL SHAREHOLDERS

As at 30th June 2002, the register of substantial shareholders maintained under Section 16(1) of the SDI Ordinance shows that, other than the interests disclosed in "Directors' interests in shares" above in respect of Ms. Qian Yuanying's interest in the Company through YY Holdings Limited, the Company has not been notified of any other interests representing 10% or more of the Company's issued share capital.

## ■ PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

There has been no purchase, sale or redemption of any of the Company's listed securities by the Group during the six months ended 30th June 2002.

## ■ AUDIT COMMITTEE

The Audit Committee has reviewed the accounting principles and practices adopted by the Group and discussed auditing, internal control and financial reporting matters, including the review of the interim financial statements which has not been audited.





## ■ CODE OF BEST PRACTICE

None of the directors is aware of any information that would reasonably indicate that the Company is not, or was not for any part of the six months ended 30th June 2002, in compliance with the Code of Best Practice as set out in Appendix 14 of the Listing Rules.

By order of the Board  
**Jiang Quanlong**  
*Chairman*

Hong Kong, 19th September 2002